

COMMITTEE ON LEGISLATIVE RESEARCH  
OVERSIGHT DIVISION

**FISCAL NOTE**

L.R. No.: 5013-01  
Bill No.: HB 1254  
Subject: Taxation and Revenue - Income; Corporations  
Type: Original  
Date: February 3, 2014

---

Bill Summary: This proposal would provide an amnesty for certain delinquent taxes, and would allow a 50% exemption from tax for the income of eligible small businesses.

**FISCAL SUMMARY**

<b>ESTIMATED NET EFFECT ON GENERAL REVENUE FUND</b>			
<b>FUND AFFECTED</b>	<b>FY 2015</b>	<b>FY 2016</b>	<b>FY 2017</b>
General Revenue	(Less than \$346,848,643)	(Less than \$346,966,438)	(Less than \$346,967,189)
<b>Total Estimated Net Effect on General Revenue Fund</b>	<b>(Less than \$346,848,643)</b>	<b>(Less than \$346,966,438)</b>	<b>(Less than \$346,967,189)</b>

Numbers within parentheses: ( ) indicate costs or losses.  
This fiscal note contains 15 pages.

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2015	FY 2016	FY 2017
Conservation Commission	Unknown	\$0	\$0
Parks, and Soil and Water	Unknown	\$0	\$0
<b>Total Estimated Net Effect on <u>Other</u> State Funds</b>	<b>Unknown</b>	<b>\$0</b>	<b>\$0</b>

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2015	FY 2016	FY 2017
<b>Total Estimated Net Effect on <u>All</u> Federal Funds</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2015	FY 2016	FY 2017
General Revenue	2 FTE	2 FTE	2 FTE
<b>Total Estimated Net Effect on FTE</b>	<b>2 FTE</b>	<b>2 FTE</b>	<b>2 FTE</b>

- ☐ Estimated Total Net Effect on All funds expected to exceed \$100,000 savings or (cost).
- ☒ Estimated Net Effect on General Revenue Fund expected to exceed \$100,000 (cost).

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2015	FY 2016	FY 2017
Local Government	\$0	\$0	\$0

### FISCAL ANALYSIS

#### ASSUMPTION

##### Section 32.383, RSMo. - Tax Amnesty Program

This part of the proposal would grant amnesty from assessment of payment of penalties, additions to tax, and interest on taxes administered by the Department of Revenue (DOR) under chapters 32, 143, 144, and 147 from August 1, 2014 to October 31, 2014. Amnesty would only apply to those tax liabilities due but unpaid on or before December 31, 2013. This section includes an emergency clause.

Officials from the **Office of Administration - Division of Budget and Planning (BAP)** assume this part of the proposal would have no fiscal impact on their organization. BAP officials noted this proposal appears to be similar to the amnesty program in FY 2003. BAP officials estimated that \$75 million in revenues would be collected, including \$50 million already identified from DOR investigations completed or in process. BAP officials stated the \$50 million is considered part of the revenue base when the consensus revenue estimates are determined for current and future years. BAP officials assume the remaining \$25 million would be "new" revenues not previously identified. Of these figures, an estimated 84.2% would be due to the General Revenue Fund, based on the results of the amnesty program in FY 2003. BAP officials also noted a small amount of taxes due to other funds might be collected if other types of delinquent taxes such as tobacco taxes are included in the amnesty.

ASSUMPTION (continued)

Further, BAP officials assume the proposed amnesty would persuade taxpayers to settle accounts in a more timely fashion than is typical. Based on data provided by DOR, BAP officials estimated 27% of liabilities collected are settled within nine months of being identified by the DOR, with others taking up to 36 months or more to settle. BAP officials assume the amnesty program would bring all of these payments into the three-month amnesty window. This would have an additional positive cash flow impact in FY 2015, at the expense of payments that would have otherwise been received in later years.

BAP assumes this proposal would increase collections in FY 2015, with impacts on later years as noted in the following table.

All funds

	Total	<b>2015</b>	2016	Later Years
Amnesty collections	75.0	<b>75.0</b>		
Normal collections	(50.0)	<b>(13.6)</b>	(22.8)	(13.6)
Difference	25.0	<b>61.4</b>	(22.8)	(13.6)

General Revenue Fund

	Total	<b>2015</b>	2016	Later Years
Amnesty collections	63.2	<b>63.2</b>		
Normal collections	(42.1)	<b>(11.4)</b>	(19.2)	(11.5)
Difference	21.1	<b>51.8</b>	(19.2)	(11.5)

Officials from the **Department of Revenue (DOR)** assume this part of the proposal could have a net positive impact on the General Revenue Fund of \$51.8 million based on Total State Revenue in fiscal year 2013 of \$61.4 million. DOR officials estimated that a total of \$75 million (\$63 million to the General Revenue Fund) could be received through amnesty, but a total of \$50 million (\$42 million to the General Revenue Fund) would have been identified as outstanding liabilities by DOR. DOR officials also assume an overwhelming majority of the \$50 million, plus interest and penalties, could be collected without amnesty.

ASSUMPTION (continued)

Because DOR has processes and personnel in place to collect delinquent taxes, the \$50 million is taken into consideration when the consensus revenue estimates are determined.

DOR officials noted there are approximately 377,000 known taxpayers eligible for amnesty. The postage, envelopes and printing costs for notification of those filers is calculated as  $377,000 \times \$0.555 = \$207,350$ .

- \* Existing staff working overtime would be used to complete correspondence at a cost of \$78,540.
- \* Existing staff working overtime would be used to complete error corrections at a cost of \$57,3324.
- \* Personal Tax would use temporary employees for processing returns, and temporary employees and existing staff working overtime to process payments.
- \* Business Tax would use existing staff working overtime to process returns and payments at a cost of \$113,883.
- \* Collections and Tax Assistance would use temporary employees for customer contacts at a cost of \$23,562.

DOR officials also recommended an advertising budget of at least \$400,000; DOR officials assume advertising the amnesty program would enhance overall participation in the program. Advertising could also help ensure that individuals and businesses not already in contact with DOR about their tax liabilities participate in the program.

DOR officials provided an estimate of the IT cost to implement this part of the proposal. The DOR estimate of IT cost is \$74,474 for 2,728 hours of programming to make changes to DOR tax systems.

**Oversight** assumes the amnesty program would be implemented as part of a broader upgrade of DOR collections and customer service programs. Accordingly, Oversight will indicate unknown costs in excess of \$100,000 in FY 2015 for the Department of Revenue to administer the amnesty program.

ASSUMPTION (continued)

**Oversight** notes this proposal would require DOR to deposit all collections from the amnesty program, except for those which are earmarked by the Missouri Constitution, into the General Revenue Fund. Therefore, taxes normally deposited to other state funds, such as the State School Moneys Fund, and for local governments may be deposited into the General Revenue Fund instead, if this proposal is enacted.

**Oversight** assumes in all cases, delinquent taxes collected would be significantly greater than the penalties, interest, and additions to tax waived, and will indicate additional revenues for the state General Revenue Fund in excess of \$100,000, in addition to the recovery of program costs for FY 2015. Oversight will indicate unknown positive fiscal impact for the Conservation Commission Fund and the Parks and Soils and Water Fund for FY 2015.

Section 143.013, RSMo. - Business Income Deduction:

Beginning January 1, 2014, this part of the proposal would allow a taxpayer to subtract 50 percent of income from eligible small businesses from federal adjusted gross income when determining Missouri adjusted gross income.

Officials from the **Office of Administration - Division of Budget and Planning (BAP)** assume this part of the proposal would have no fiscal impact to their organization.

The proposal would define business income as income greater than zero arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations.

BAP officials noted there does not appear to be language requiring this income to be Missouri source income, so the estimates below are larger than in other similar bills. BAP officials estimated the annual costs of the reductions for individuals for small business income as \$264 million, and the annual costs of the reduction for corporations would be \$180 million. BAP officials noted they do not have sufficient data at this time to refine these estimates based on the specific levels of proposed income.

This proposal would be effective for tax years beginning on or after January 1, 2014, therefore this provision would reduce FY 2015 revenues.

ASSUMPTION (continued)

BAP officials also noted it is very difficult to identify business income from available data. If the proportion of taxable income that is business income is greater than that estimated for this analysis, then the loss of revenues would be higher. Also, BAP officials noted this analysis makes no attempt to quantify the loss of revenues that might occur if taxpayers alter their filing status to take advantage of the business income subtraction.

Officials from the **Department of Revenue (DOR)** stated for calendar year 2011, individual income tax filers reported \$14.4 billion in business income on their federal Form 1040s. DOR officials included the total reported on Schedule C and Schedule E in the calculation. The \$14.4 billion does not include those returns filed by nonresidents where the federal information is not available. For calendar year 2011, Missouri corporate taxpayers reported \$5.8 billion in taxable income and \$361.4 million in tax. DOR officials stated they were unable to determine the amount of corporate taxpayers that have a net income that does not exceed \$500,000.

Fiscal impact

DOR officials estimated this proposal would result in an annual reduction in revenue of \$434.4 million. However, this number may be highly overstated, because DOR cannot determine the number of eligible c-corporations with a net income that does not exceed \$500,000.

Administrative impact

DOR officials assume Personal Tax would require two additional Temporary Tax Employees for key entry and two additional Revenue Processing Technicians I for error correction and correspondence. The Corporate Tax Division would require form changes in addition to identifying and submitting COINS programming changes to ITSD and testing the required changes to verify the deduction is functioning properly. Collections and Tax Assistance (CAOA) would anticipate receiving a significant number of customer contracts and contacts on notice of adjustment. This would require two additional Tax Collection Technicians I for contacts to the delinquent and non-delinquent lines and one additional Revenue Processing Technician I for contacts to the field offices.

ASSUMPTION (continued)

The DOR estimate of administrative cost to implement this proposal included five additional employees and two additional temporary tax employees. The total cost to implement the tax exemption for 50% of eligible small business income included in this proposal, including additional employees and related equipment and expense was \$229,177 for FY 2015, \$221,598 for FY 2016, and \$223,918 for FY 2017.

**Oversight** assumes the DOR estimate of expense and equipment cost for the new FTE could be overstated. If DOR is able to use existing desks, file cabinets, chairs, etc., the estimate for equipment could be reduced by roughly \$6,000 per new employee.

**Oversight** assumes the business income tax exemption could be implemented with two additional employees and has, for fiscal note purposes only, changed the starting salary for the additional employees to correspond to the second step above minimum for comparable positions in the state's merit system pay grid. This decision reflects a study of actual starting salaries for new state employees and policy of the Oversight Subcommittee of the Joint Committee on Legislative Research. Oversight has also adjusted the DOR estimate of equipment and expense in accordance with OA budget guidelines. Finally, Oversight assumes a limited number of additional employees could be accommodated in existing office space.

IT impact

DOR officials assume the IT cost to implement this portion of the proposal would be \$27,518 based on 1,008 hours of programming to make changes to various tax systems.

**Oversight** assumes OA - ITSD (DOR) is provided with core funding to handle a certain amount of activity each year. Oversight assumes OA - ITSD (DOR) could absorb the costs related to this proposal. If multiple bills pass which require additional staffing and duties at substantial costs, OA - ITSD (DOR) could request funding through the appropriation process.

Officials from the **University of Missouri - Economic and Policy Analysis Research Center (EPARC)** stated the proposal would define "taxpayer" as "any eligible C-corporation or eligible small business." Further, an "Eligible C-corporation" would be eligible for the 50% exemption as long as it has a net income not exceeding \$500,000 and an "Eligible Small Business" would be eligible for the 50% exemption as long as it has a net income not exceeding \$100,000.



ASSUMPTION (continued)

EPARC officials noted they possess data to indicate the amount of taxable income for each corporation, but do not possess the data to discern corporation or business types within our corporate database. Therefore, EPARC was unable to prepare an estimate of impact for this legislation.

Bill as a Whole

Officials from the **Joint Committee on Administrative Rules** assume there is no fiscal impact from this proposal.

Officials at the **Missouri Veterans Commission** assume the impact to their organization is unknown.

Officials from **St. Louis County** assume there would be no fiscal impact to their organization from this proposal.

Officials from the **Office of the Secretary of State (SOS)** stated many bills considered by the General Assembly include provisions allowing or requiring agencies to submit rules and regulations to implement the act. The SOS is provided with core funding to handle a certain amount of normal activity resulting from each year's legislative session. The fiscal impact for this fiscal note to the SOS for Administrative Rules is less than \$2,500. The SOS recognizes that this is a small amount and does not expect that additional funding would be required to meet these costs. However, the SOS also recognizes that many such bills may be passed by the General Assembly in a given year and that collectively the costs may be in excess of what the office can sustain with the core budget. Therefore, the SOS reserves the right to request funding for the cost of supporting administrative rules requirements should the need arise based on a review of the finally approved bills signed by the governor.

Oversight assumptions

**Oversight** notes this proposal would provide a 50% exemption from tax for certain eligible C corporations and for the eligible business income reported by individuals. The proposal would allow the deduction from the taxpayer's adjusted gross income.

ASSUMPTION (continued)

Individual business income deduction

**Oversight** notes this proposal would allow an individual to deduct 50% of business income from a business, including a proprietorship, partnership, S corporation, limited liability company, or limited liability partnership, provided that business is subject to tax and has a net income less than \$100,000 per year.

Oversight assumes this proposal would be implemented by allowing the owners of the businesses to deduct 50% of income attributed to them by the eligible small business.

In response to SB 496 LR 4416-01, officials from the **University of Missouri, Economic Policy Analysis and Research Center (EPARC)** assumed that, if enacted, that proposal would phase in a 50% “business income” subtraction for individual taxpayers’ business income as defined in the proposal.

EPARC officials began by enumerating “business income” for the Missouri 1040. Business income was assumed to equal self-employment income and was calculated by dividing each filer’s self-employment tax by the applicable tax rate. This process resulted in an estimated aggregate positive “business income” of \$7,665,022,747 for 312,404 Missouri filers.

EPARC officials then applied a percentage of that business income in their simulations to estimate the impact of the proposal; a 10% subtraction for 2014, a 20% subtraction for 2015, a 30% subtraction for 2016, a 40% subtraction for 2017 and a 50% subtraction for 2018.

**Oversight** notes the EPARC simulation for 2018 included a full 50% reduction in business income which resulted in a simulated reduction in net tax due of \$147,925,000; Oversight assumes the current proposal would result in a revenue reduction less than \$147,925,000 due to the income limitation for the small business.

Corporate income deduction

**Oversight** notes the determination of adjusted gross income is not applicable to corporations, but assumes the proposal could be implemented by allowing a 50% deduction from taxable income as currently defined for corporations subject to tax and having net income less than \$500,000 per year.

ASSUMPTION (continued)

**Oversight** notes that officials from the **University of Missouri, Economic Policy Analysis and Research Center (EPARC)** provided a baseline simulation of corporate income tax of \$397,939,000 based on current provisions and the most recent available data from 2011.

Oversight notes the impact of this proposal, if implemented by allowing a 50% deduction of taxable income as currently defined for eligible small businesses, would be a revenue reduction less than  $(\$397,939,000 \times 50\%) = \$198,969,500$  and will include that impact in this fiscal note.

<u>FISCAL IMPACT - State Government</u>	FY 2015	FY 2016	FY 2017
<b>GENERAL REVENUE</b>			
<u>Additional Revenue - DOR</u>			
Tax Amnesty Section 32.383	More than \$100,000	\$0	\$0
<u>Cost - DOR</u>			
Tax amnesty program Section 32.383	(More than \$100,000)	\$0	\$0
<u>Revenue Reduction - DOR</u>			
Business income exemption Section 143.013			
Individuals	(Less than \$147,925,000)	(Less than \$147,925,000)	(Less than \$147,925,000)
Corporations	(Less than \$198,969,500)	(Less than \$198,969,500)	(Less than \$198,969,500)
<u>Cost - Department of Revenue</u>			
Income tax changes Section 143.011			
Salaries	(\$23,136)	(\$46,272)	(\$46,735)
Benefits	(\$11,801)	(\$23,601)	(\$23,837)
Equipment and expense	<u>(\$19,206)</u>	<u>(\$2,065)</u>	<u>(\$2,117)</u>
Total cost - DOR	(\$54,143)	(\$71,938)	(\$72,689)
FTE change - DOR	2 FTE	2 FTE	2 FTE
<b>ESTIMATED NET EFFECT ON GENERAL REVENUE</b>	<b>(Less than <u>\$346,848,643</u>)</b>	<b>(Less than <u>\$346,966,438</u>)</b>	<b>(Less than <u>\$346,967,189</u>)</b>
Estimated Net FTE impact on General Revenue Fund	2 FTE	2 FTE	2 FTE

FISCAL IMPACT - State Government  
(Continued)

FY 2015

FY 2016

FY 2017

**CONSERVATION COMMISSION**

Additional Revenue - DOR

Tax Amnesty

Section 32.383

Unknown

\$0

\$0

**ESTIMATED NET EFFECT ON  
CONSERVATION COMMISSION**

Unknown

\$0

\$0

**PARKS, AND SOIL AND WATER  
FUNDS**

Additional Revenue - DOR

Tax Amnesty

Section 32.383

Unknown

\$0

\$0

**ESTIMATED NET EFFECT ON  
PARKS, AND SOIL AND WATER**

Unknown

\$0

\$0

FISCAL IMPACT - Local Government

FY 2015

FY 2016

FY 2017

\$0

\$0

\$0

### FISCAL IMPACT - Small Business

This proposal would reduce income taxes on small businesses and their owners.

### FISCAL DESCRIPTION

This bill would authorize an amnesty from the assessment or payment of penalties, additions to tax, and interest on delinquencies of unpaid taxes administered by the Department of Revenue which existed on or prior to December 31, 2013. A taxpayer would be required to apply for amnesty; pay the unpaid taxes in full between August 1, 2014, to October 31, 2014; and agree to comply with state tax laws for the next eight years from the date of the agreement. A taxpayer who is granted amnesty would not be eligible to participate in any future amnesty for the same tax. All tax payments received from the tax amnesty program would be deposited into the General Revenue Fund unless otherwise earmarked by the Missouri Constitution.

Beginning January 1, 2014, an eligible small business or eligible corporation would be allowed a 50% deduction for small business income. To be eligible, net income for a corporation could not exceed \$500,000 and net income for small business could not exceed \$100,000. Business income would not include compensation or income from farming or agribusiness activities. A shareholder of a S-corporation, a member of a limited liability company or limited liability partnership, and a partner in a partnership would be allowed a flow-through deduction.

The tax amnesty would expire December 31, 2021, and the tax amnesty provisions include an emergency clause.

This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

Department of Revenue  
Joint Committee on Administrative Rules  
Missouri Veterans Commission  
Office of Administration  
    Division of Budget and Planning  
Office of the Secretary of State  
St. Louis County  
University of Missouri  
    Economic and Policy Analysis Research Center

Mickey Wilson, CPA  
Director  
February 3, 2014



Ross Strobe  
Assistant Director  
February 3, 2014